

# DEFENSE SYSTEMS MANAGEMENT COLLEGE

## FUNDS MANAGEMENT DEPARTMENT

AUG 00

### TEACHING NOTE

## PROGRAM EXECUTION

### SIOBHAN TACK

### APPORTIONMENT PROCESS

After Congress has granted budget authority via an appropriations act, the budget authority is released for execution via the *apportionment* process. The intent of apportionment is to achieve the most effective and economical use of the funds made available. Funds are apportioned by the Office of Management and Budget (OMB) to federal government agencies and departments on a quarterly, annual, or other periodic basis. Investment appropriations (e.g., procurement and military construction) are usually apportioned on an annual basis, while expense appropriations (e.g., operations & maintenance and military personnel) are usually apportioned on a quarterly basis.

### Impoundment

Funds may be identified for *impoundment*, whereby the executive branch prevents budget authority from being executed. A *deferral* is a temporary impoundment of funds (e.g., due to technical problems or schedule slip), whereas a *rescission* is a permanent impoundment of funds (e.g., due to program cancellation). Under the Budget and Impoundment Control Act of 1974, the President must notify Congress of any intention not to spend appropriated funds. In the case of a rescission, Congress has 45 days of continuous session to rescind the funds by enacting a rescission bill. If Congress does not do so, the President must release the funds. If the President proposes a deferral, the funds can be withheld for up to 12 months unless either house adopts an impoundment resolution that disapproves the deferral of funds.

### Allocation

During the apportionment process the Undersecretary of Defense (Comptroller) (USD(C)) *allocates* DoD's budget authority to the various military services and defense agencies based on the appropriations made by Congress. During this process, some funds may be withheld. In the case of acquisition programs, the Undersecretary of Defense for Acquisition, Technology & Logistics (USD(AT&L)) may propose technical withholds on programs that need further review (DAB, Milestones, etc.). USD(C) analysts then prepare forms that release the initial allocation of funds reflecting the funds that are on withhold and the funds that can be obligated. These forms are signed by the Comptroller and countersigned by USD(AT&L). Once the services and defense agencies receive their allocations of funds, their comptrollers will sub-allocate the funds to major

commands or program executive offices, who will subsequently *allot* funds to their subordinate program offices for execution.

## **EXECUTION PROCESS**

With the release of funds at the local level, the following sequence of events normally takes place. Upon receipt of some form of request (e.g., Procurement Request, Purchase Order, etc.) for a spending action such as a contract, the comptroller will execute a *commitment*, or an "administrative reservation" of funds for the purpose requested. When reviewing the funds for a commitment, the comptroller will *certify* that the funds requested are available in the amount requested, of the correct fiscal year, and are of the correct appropriation for the work to be done. An *obligation* is the "legal reservation" of funds tying the government to a liability, e.g., a contract for goods or services. An *expenditure* is payment of some or all of an obligation and is generally considered to be defined as the issuing of a check. An *outlay* is a payment by the Treasury when the check is cashed. Allocations, commitments, obligations, and expenditures are carefully controlled to avoid over-spending and to track actual fiscal progress against plan.

## **PROGRAM EXECUTION**

### **Contract Administration and Payment**

Every contract specifies who will administer the contract, the terms and conditions under which payments will be made, and who will make the payments. When the contract is signed and distributed, copies go to the finance office to record the obligation, to the paying office to authorize payment, and to the contract administration office to monitor performance and process payment documents. In the current environment, Integrated Product Teams (IPTs) play a central part in helping to determine the contractor's payment, within the context of his performance or compliance with the contract. Examples of this IPT role would be: (a) determining the amount of an award fee payment; and (b) deciding on acceptance and payment for a delivered end item.

Payments may be made periodically, usually monthly, as the contractor incurs costs and invoices them under cost type contracts or as progress payments under fixed price contracts, or when the contractor delivers items specified under the contract. The contractor prepares the requisite standard forms, e.g., Contractor's Request for Progress Payment (SF 1443), provides any supporting documentation needed, and submits it to the Administrative Contracting Officer (ACO). When delivering an item for acceptance, the contractor must also submit a Material Inspection and Receipt (DD 250), a Letter of Transmittal, and any other document required by the contract. The ACO may ask the Defense Contract Audit Agency (DCAA) for an audit of the invoice. An audit is usually performed where reimbursement for costs is involved.

After the contract-administering agency has completed all actions required, the certified invoice and supporting documentation (e.g., signed DD 250) will be forwarded for payment to the paying office designated in the contract. Prior to making payment, the paying office will ensure that budget authority has been properly obligated and is sufficient to cover the invoiced amount.

The paying office will then prepare a check for the contractor and a public voucher with the funds citation. The check, when cleared through the Federal Reserve System, results in an outlay from the General Fund of the Treasury. Information for the official accounting records is drawn from the public vouchers and entered into the Defense Finance & Accounting Service (DFAS) automated accounting systems.

The payment system is not conceptually complicated; in practice, however, paying and accounting for payments may be a lengthy and complex process. Progress payments are not automatic but require an assessment of progress to date, normally by the Defense Contract Management Command (DCMC) or another administering agency, before payment is made. In fact, given inadequate performance, payment may be withheld in part or in full. Acceptance procedures for deliverables may also be extensive. In preparing invoices, standard forms, and other supporting documentation, the contractor may provide insufficient and/or incorrect information. Errors in documentation lead to rejections that must be corrected and reprocessed.

Insufficiency of obligated funds or failure to find a matching obligation (e.g., due to incorrect citation of funds) will delay payment. Delays in accounting for payments may take months, primarily to find and correct errors. Inaccurate accounting reports increase the already difficult execution problems facing program offices. Resolving errors and unsnagging delays in accounting, while not actually performed by the program office, nonetheless consume a great deal of program office time due to the need to closely track the resolution of problems. Accounting delays can give the appearance of program delays and excess program funds. This situation may cause the program to be targeted as a source of funds for reprogramming actions.

### **Contract Funds Status Report**

The Contract Funds Status Report (CFSR) (DD 1586) is used to obtain funding data on contracts over six months in duration. The CFSR provides DoD Components with information to assist in updating and forecasting contract funds requirements, planning and decision making on funding changes, developing funds requirements and budget estimates in support of approved programs, and determining funds in excess of contract needs and available for deobligation.

No specific CFSR application thresholds are established; however, applications to contracts of less than \$1.2 million (FY 1996 constant dollars) are evaluated carefully to ensure that only the minimum information necessary for effective management control is required. The CFSR is not applied on firm fixed price contracts unless unusual circumstances require specific funding visibility. For example, the CFSR may be applied to unpriced portions of firm fixed price contracts that individually or collectively are estimated by the DoD Component to exceed 20% of the initial contract value. In such cases, the contract specifies CFSR requirements to be imposed on the contractor to fit the individual circumstances.

## **MISAPPROPRIATION ACT**

Title 31, U.S. Code, Section 1301, dealing with the application of monies appropriated by Congress, requires that funds be used only for the programs and purposes for which the appropriation is made. An example of a violation of the Misappropriation Act is the use of a Procurement appropriation for an effort that should properly be funded with a Research, Development, Test & Evaluation (RDT&E) appropriation (e.g., LRIP articles to be used for testing purposes). Another example is using Operations and Maintenance (O&M) funds to buy an item whose system unit cost exceeds the \$100K threshold set by Congress. Such items should be purchased with procurement funds.

Violations of the Misappropriation Act can be avoided by properly reprogramming funds (see “Reprogramming” below).

## **ANTIDEFICIENCY ACT**

Title 31, U.S. Code, Sections 1341 and 1517 are probably the most important statutes affecting spending obligations at the activity level. The main provisions of these sections:

- a. Prohibit any officer or employee from making or authorizing an obligation in excess of the amount available in an appropriation or in excess of the amount permitted by agency regulations.
- b. Forbid the government from obligating funds in advance of appropriations.
- c. Require the head of each agency to issue regulations establishing an administrative control system both to keep obligations within the amount of apportionment, and to enable the agency to fix responsibility for making obligations in excess of the apportionment.

Some examples of violations of Sections 1341 and 1517 are:

- Actions, including clerical recording or reporting error, that result in an over-commitment, over-obligation, or over-expenditure of funds in any appropriation.
- An official who involves the government in a contract or obligation either in advance of appropriations or without adequate funding authority.
- Attempts to avoid an over-obligation or over-expenditure by failure to post to accounting records; by delay in posting until funds are received; by not properly charging the appropriated fund; or by transferring charges or funds between accounts. Whether an over-obligation or over-expenditure had actually occurred in the above circumstances would depend upon the results of corrective actions.

## **BONA FIDE NEED RULE**

Section 1502(a) of Title 31, U.S. Code states that, "The balance of an appropriation or fund limited for obligation to a definite period is available only for payment of expenses properly incurred during the period of availability, or to complete contracts properly made within that period of availability and obligated consistent with section 1501 of this title."

Simply stated, this ***Bona Fide Need*** rule requires that appropriated funds be used only to obtain goods and services for which a need arises during the period of the appropriation's availability for obligation.

Some examples of Bona Fide Need include:

- Supply items: Generally, bona fide need is determined by when the government actually requires (will be able to use) the supplies being acquired. Supply needs of a future year are the bona fide need of the year in which they are required, unless an exception applies.
  - Lead-time exception: Agencies are permitted to consider normal production lead-time in determining bona fide need for an acquisition. E.g., if the normal lead-time for an item is 30 days, the government may obligate FY98 funds for an item required on or before 30 Oct 98.
  - Stock level exception: Agencies may use current year funds to replace stock consumed in the current fiscal year, even though the replacement stock will not be used until the following fiscal year. However, fiscal-year-end stockpiling of supplies in excess of normal usage requirements is prohibited.
- Service contracts: Generally, services are the bona fide need of the fiscal year in which they are performed. Thus, service contracts have not normally been permitted to cover a period which involves two different fiscal years. However, two important exceptions exist to this general rule:
  - Nonseverable services exception. If the services produce a single or unified outcome, product, or report, the services are nonseverable and the government may fund the entire effort with dollars available for obligation at the time the contract is executed, and the contract execution may cross fiscal years.
  - Statutory exceptions: The FY98 Defense Authorization Act amended 10 USC 2410a to permit authorized DoD agencies to obligate funds available at the time of contract award to finance any severable service contract with a period of performance of up to one year. Previously, this permission had been limited to certain types of contracts

- Construction contracts: Work must commence prior to 15 December to be considered as a bona fide need of the prior fiscal year. The government should also consider normal lead-time, normal weather conditions, and factors within government control (e.g., site access availability) in determining bona fide need.
- Weather conditions: A project that cannot reasonably be expected to commence before the onset of winter weather is not a bona fide need of the prior fiscal year.
- Factors within government control: In considering bona fide need, the government must consider the required delivery date, the normal rate of construction, when the government intends to make facilities, sites, or tools available, and the degree of control the government has over when the contractor may begin work.

## **REPROGRAMMING**

Reprogramming is the use of funds for purposes other than those contemplated by the Congress at the time originally appropriated. These actions do not represent requests for additional funds from the Congress. Rather, they normally involve the reapplication of resources within the budget authority already appropriated from a *source* to an *increase*. Reprogramming guidance is contained in the DoD Financial Management Regulation (DoD 7000.14-R), Volume 3, Chapter 6.

### **Types of Reprogramming Actions**

*(Note: As of 12 Nov 1999, DoD's reprogramming procedures were changed to include just three types of reprogramming actions: Congressional prior approval, internal, and below-threshold. Actions previously classified as congressional notification reprogrammings are now classified as congressional prior approval actions.)*

***Congressional prior approval reprogramming*** applies to actions:

- 1) Requesting procurement quantity increases for major end items;
- 2) Affecting matters of special interest to one or more committees, regardless of the dollar amount;
- 3) Involving use of the Secretary of Defense's general transfer authority (i.e., movement of funds *between* appropriations);
- 4) Exceeding the thresholds specified in **Figure 1** for reprogrammings between elements at the specified level of control (e.g., between program elements within an RDT&E appropriation or between line items within a procurement appropriation);
- 5) Involving new starts:
  - a) Establishing a new procurement program, procurement subprogram, RDT&E program, RDT&E project, or RDT&E subproject estimated to cost \$10 million or more within the first 3 years.
  - b) Any new modification except safety modifications costing less than \$10 million.
- 6) Establishing new line items (for any program year):

- a) New procurement line item of \$2 million or more.
- b) New RDT&E program element, project, or subproject of \$2 million or more.
- 7) Terminations which:
  - a) Eliminate a procurement program or subprogram of \$10 million or more.
  - b) Eliminate an RDT&E program element, project, or subproject which is equal to the total amount of the program element.
  - c) Eliminate an RDT&E project or subproject within a program element of \$10 million or more.

DoD submits requests for prior approval reprogrammings on DD Form 1415-1. Requests involving use of general transfer authority must be approved by OMB prior to transmittal to the congressional committees (the House and Senate Armed Services Committees (HASC and SASC) and the House and Senate Appropriations Committees (HAC and SAC). The congressional committees must each provide approval in letter format for the sources and increases requested in the prior approval reprogramming request. The committees may disapprove specific increases or sources requested or change the amount allowed for a requested increase or source. OSD weights each committee's response equally and implements the lowest of the approvals received for both proposed sources and increases via memorandum to the affected DoD Component(s).

Most prior approval reprogramming requests are consolidated by each service/defense agency for submission as part of the annual DoD "omnibus" reprogramming submission. However, in urgent cases, DoD may forward an individual prior approval reprogramming request addressing a specific requirement outside of the omnibus request.

***Internal reprogramming*** is requested on DD Form 1415-3 and requires approval by the USD(Comptroller) (USD(C)). Internal reprogramming creates an audit trail and documents actions that do not involve changes from the purposes and amounts justified in the budget presentations to the Congress or to funds that Congress has added to programs during the enactment process. Funds may be internally reprogrammed to reclassify them for proper execution in a different line item or appropriation than that appropriated. If the realignment of funds requires a change of appropriations, then general transfer authority must be used and OMB approval must be obtained after signature of the DD 1415-3 by USD(C). Funds may also be internally reprogrammed to or from ***transfer accounts***. Transfer accounts established by Congress are appropriations that contain funds which are to be transferred to other appropriations for execution. An example of a transfer account is the Environmental Restoration, Defense appropriation. The funds provided in this appropriation are internally reprogrammed to appropriate procurement, RDT&E, O&M or MILCON appropriations for use on environmental projects.

***Below threshold reprogramming*** is approved by the individual services and defense agencies. This includes all actions that do not meet the criteria for prior approval or internal reprogramming.

**Below-Threshold Reprogramming**  
**Prior Approval required if amount equals or exceeds**

APPN CAT	INCREASE	DECREASE	LEVEL OF CONTROL
RDT & E	+ \$ 4 M	Greater of - \$ 4 M - 20 %	PROGRAM ELEMENT
PROC	+ \$ 10 M	Greater of - \$ 10 M - 20 %	LINE ITEM
O & M	+\$ 15 M	No restriction, unless otherwise specified	BUDGET ACTIVITY SOME BA 1 SUB-ACTIVITY LIMITATIONS ON DECREASES (OPERATING FORCES)
MILPERS	+\$ 10 M	No Congressional Restriction	BUDGET ACTIVITY
MILCON	Lesser of + \$ 2 M + 25 %	No Congressional Restriction	PROJECT

Reference Source: Memo Change (12 Nov 99) to DoD Financial Management Regulation, Volume 3.

**Figure 1**

**EXPIRATION AND CANCELLATION OF FUNDS**

Each appropriation has a legal time limit within which to obligate funds. These limits are:

<u>Appropriation Category</u>	<u>Years</u>
RDT&E	2 years
Procurement (excluding SCN)	3 years
SCN (Shipbuilding & Conversion Navy)	5 years
Operation & Maintenance	1 year
MILPERS	1 year
MILCON	5 years

Budget authority that remains following these periods is said to have "expired", but can it still be used?

**Legislative Background**

In 1956 Congress authorized agencies to retain the use of their unused budget authority. Each agency became solely responsible for all disbursements against its obligations, and additionally, could use the unobligated budget authority to fund amounts above the original obligation. Rules and a framework for managing this unused budget authority, which the law named "merged" and "merged surplus authority" (M) accounts, were established in Title 31, U.S. Code, Sections 1551 through 1557.



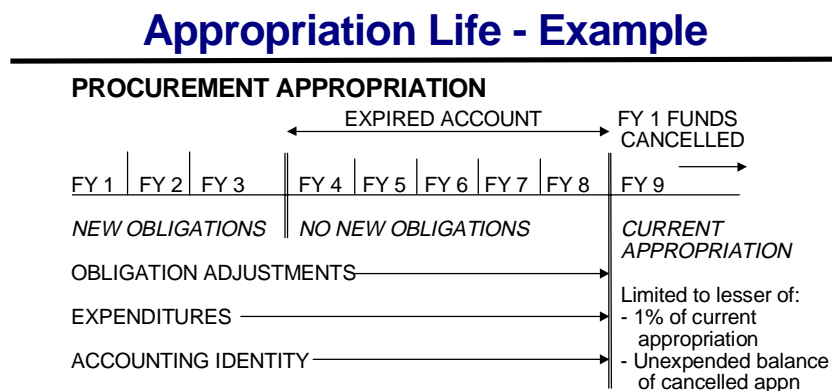
Congressional involvement and oversight were not required by the 1956 law. When the defense budget grew significantly during the mid-1980s, the M account balances swelled into the billions. The highly visible usage of the merged account by the B-1B program created concern within Congress that DoD was complying with the letter but not the intent of the law.

## Congressional Changes

As a result of this increased congressional interest, The National Defense Authorization Act for FY 1991 mandated changes to Title 31. The legislation set up a transition period leading to the elimination of the M accounts by the end of FY 1993, established a new **expired** account structure, and limited the use of expired funds for contract adjustments.

The changes to Title 31 did not affect an appropriation's period of availability for new obligations. Following an appropriation's legal time limit for new obligations, the unexpended balances (both obligated and unobligated) are transferred to "expired" accounts (maintained by the agencies), where they remain for five years. As before, this expired budget authority maintains all of its original accounting identity (appropriation, fiscal year, line item, etc.), and remains available for obligation adjustments and payments. However, after the five-year period ends, the remaining unexpended balances are **cancelled** and cannot be restored. Thereafter, upward obligation adjustments and payments related to the cancelled appropriation must be funded with appropriations currently available for the same purpose. Use of current appropriations to fund adjustments against cancelled appropriations is limited to the lesser of: (1) one percent of the total currently available appropriation; or (2) the unexpended balance of the cancelled appropriation. In other words, regardless of the availability of one percent of the current appropriation, the original appropriation can never be exceeded.

**Figure 2** illustrates these rules for a generic Procurement appropriation (not SCN) originally appropriated in FY1. The appropriation is available for new obligation purposes (is **current**) through the end of FY3. At the end of FY3, the appropriation becomes **expired** and all unexpended balances (obligated and unobligated) are placed in an expired account. At the end of FY8, the remaining unexpended balances of the appropriation are **cancelled**. From FY9 on, any obligation adjustments or payments related to the original FY1 procurement appropriation must be funded by procurement appropriations currently available for the same purpose.



**Figure 2**

Upward obligation adjustments are increases in the original obligations and result from contractually driven future events. The general rule for determining if original year funds can be used is whether the change is within the scope of the original contract. Within-scope adjustments would include charges against expired funds for such items as contingent liabilities (e.g., award fees, price inflation), reprocurement actions, claims, and settlements. Out-of-scope adjustments would include charges against current funds for any additional work resulting in further billable costs (e.g., quantity increases, increased levels of service). With the exception of contingent liabilities, the use of expired funds for cumulative upward adjustments (for any program, project or activity) that exceed \$4 million during a fiscal year, requires USD(C) approval prior to obligation of the funds. Additionally, if these planned adjustments exceed \$25 million, DoD must submit the request in writing to the House and Senate Appropriations and Armed Services Committees under a 30-day prior notification rule.

It appears that these changes are having a significant effect on the availability of current year funds for new obligations. This is because expenditures beyond the five year expired period now have to be charged to currently available appropriations. Additionally, we become potentially liable for antideficiency violations if current funds are not sufficient and we need to request a supplemental appropriation. The DoD Financial Management Regulation (DoD 7000.14-R), Volume 3, Chapter 10 is the source for guidance on expired and canceled account implementation.

## **SUMMARY**

Once budget authority has been appropriated by Congress, and apportioned by OMB, DoD allocates funding to the Services and Defense Agencies, who then execute the funds by committing, obligating, expending, and outlaying them. During execution, financial managers must be aware of the rules governing the life of appropriations and avoid violating fiscal laws (anti-deficiency, misappropriation, and bona fide need) while making efficient use of their budget authority, which is usually evaluated based on performance relative to obligation and expenditure plans. Failure to execute funds according to plan usually results in their loss to fund some other requirement. If funds originally appropriated for one program or purpose need to be redirected to another program or purpose, DoD must comply with the reprogramming rules established by Congress.